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5 UNITED STATES BANKRUPTCY COURT  
6 NORTHERN DISTRICT OF CALIFORNIA

7 In re

8 SANTA VENETIA CENTER FOR THE  
9 ARTS AND HUMANITIES, INC.,

No. 02-12339

Debtor(s).  
\_\_\_\_\_

10 Memorandum re Sanctions  
11 \_\_\_\_\_

12 The matter of sanctions, pursuant to a motion by Chapter 7 Trustee Charles Sims and the court's  
13 own motion, is now before the court. The objects of the sanctions are Christopher Egan, the debtor's  
14 former principal, the law firm of Lanahan & Reilley, and attorney Jennifer E. Torbohn. The  
15 consideration of sanctions was triggered by blatant misrepresentations made to a state court regarding  
16 procedural deficiencies in the bankruptcy proceedings. While the state court eventually saw through the  
17 lies, considerable expense to the bankruptcy estate was involved in setting things right.

18 This case was originally commenced as a Chapter 11 on September 27, 2002. The filing was  
19 caused by a pending foreclosure by the San Rafael Unified School District, which held a deed of trust to  
20 the debtor's real property at 1565 Vendola Drive, San Rafael, California, its only significant asset.

21 The Vendola Drive property was sold to debtor Santa Venetia Center for the Arts and  
22 Humanities, Inc., in 1994 for a purchase price of \$900,000.00 plus Santa Venetia's agreement to provide  
23 20 years of qualified professional artistic services to the District's students at a minimum of 300 hours  
24 per year to assist the District in its educational program. The District took back a deed of trust securing  
25 both a note for \$810,000.00 and the obligation to provide the artistic services.

26 Before bankruptcy, Santa Venetia had fallen into default and the District had engaged in

1 negotiations with Christopher Egan, Santa Venetia's sole director and officer, about a workout.  
2 Negotiations broke down, and Egan commenced a state court action seeking to enjoin the District's  
3 foreclosure. When that action was unsuccessful, he commenced this bankruptcy case on behalf of Santa  
4 Venetia.

5 The case remained in Chapter 11 until July 30, 2003, when the court converted the case to  
6 Chapter 7 after determining that the plan proposed by Santa Venetia was insufficient to cure the non-  
7 monetary defaults to the District and lacked the required votes. The District had opposed confirmation  
8 arguing, among other things, that the sale to Santa Venetia was subject to rescission due to the failure of  
9 Santa Venetia to perform legitimate public benefit functions. Sims was then appointed Chapter 7  
10 Trustee.

11 In September, 2003, Sims and the District reached a compromise regarding their mutual rights.  
12 Under the terms of the agreement, the District would pay the Trustee \$40,000.00 and subordinate its  
13 claims in return for an agreement to rescind the purchase. Rule 2002(a)(3) of the Federal Rules of  
14 Bankruptcy Procedure requires that notice of a proposed compromise be given to all creditors and  
15 parties in interest; Local Rule 2002-1(c) of the Northern District of California requires that when notice  
16 is given by a party he must use a current set of mailing labels supplied by the court. Proper notice was  
17 given in full compliance with these rules on September 30, 2003.

18 At about the same time Egan, on behalf of Santa Venetia, moved to dismiss the bankruptcy. His  
19 motion was served using exactly the same mailing labels. On October 24, 2003, the court approved the  
20 compromise and denied the motion to dismiss.

21 The conduct which has led to the consideration of sanctions occurred in state court in mid-2004,  
22 when the District sought to recover possession of the premises from Egan and five artists who claimed  
23 lease rights through Santa Venetia. Their attorney, Jennifer Torbohn of Lanahan & Reilly, attacked the  
24 validity of the compromise this court had approved on the grounds that the compromise had not been  
25 properly noticed.

26 On June 6, 2004, Torbohn filed her declaration in the state court stating that she had reviewed the

1 bankruptcy file and it showed that the artists had been “removed as creditors” in the bankruptcy.<sup>1</sup> She  
2 failed to inform the state court that the bankruptcy files reflected that five of her six clients, including  
3 Egan, had at all times been on the bankruptcy court’s mailing list and had been served with *every* notice  
4 in the case, including the initial notice to creditors, the plan and disclosure statement, the notice of  
5 compromise and Egan’s own motion to dismiss. Based on her blatant omission of these facts, she argued  
6 to the state court that her clients had never had the opportunity to contest the compromise and it was  
7 ineffective as to them and that the District’s (correct) argument that her clients had been given proper  
8 notice “*belies the facts of the case.*” (Emphasis added).

9         It was at this point that the bankruptcy estate began to incur unexpected expenses. Egan and his  
10 cohorts, through Lanahan & Reilley, collaterally attacked this court’s order in state court by arguing that  
11 they had been deprived of their “day in court.” Sims’ counsel was forced to prepare a declaration  
12 pointing out that the bankruptcy file reflected service on Egan and the artists and explain to the state court  
13 that they had not been removed from the official mailing list, and appear in state court on August 3, 2004.  
14 On August 25, 2004, the state court rejected Lanahan & Reilley’s argument regarding notice and ruled  
15 that any attack on the compromise had to be made in bankruptcy court.

16         On August 3, 2004, Lanahan & Reilley filed a motion in this court seeking to undo the settlement  
17 based, interestingly, on alleged fraud of the District. Aside from one statement that the settlement had  
18 been consummated “unbeknownst” to them, no argument was made that notice was deficient. The court  
19 rejected the motion, noting that Egan and the artists had full notice of the compromise, failed to object at  
20 the proper time, and that there was no valid argument for revisiting the matter at this late date. Sims  
21 then followed with his motion for sanctions pursuant to FRBP 9011, seeking to recover \$2,600.00 in  
22 expenses incurred in the state court proceedings, \$3,250.00 opposing the motion in this court and  
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24         <sup>1</sup>There is no way that amendment of a schedule can deprive any person of notice. Once a person  
25 is scheduled as a creditor or interest holder, or files a proof of claim or request for notice, that person  
26 continues to receive notices unless the person requests that the court remove him or her from the official  
mailing list.

1 \$325.00 for preparing the motion. The court also issued an order to show cause why it should not assess  
2 sanctions on its own motion.

3 While the court found the motion made in this court to be without merit, the court cannot say that  
4 it is so meritless as to justify sanctions. Unlike the state court pleadings, which contained outright  
5 falsehoods, the motion made in this court made only the “unbeknownst” comment without trying to  
6 ascribe any denial of rights to it. It is not this motion which offends the court and does serious damage to  
7 the administration of justice, but rather the false representations made to the state court that this court had  
8 made a ruling without affording anyone the opportunity to be heard.

9 Without authority, Lanahan & Reilley argues that this court cannot assess sanctions for  
10 representations made in another court. There is no such authority for this assertion. If the action of  
11 counsel does damage to the administration of justice, it may be the subject of contempt proceedings even  
12 though committed far from the courtroom. *Toledo Newspaper Co. v. United States*, 247 U.S. 402, 38  
13 S.Ct. 560, 62 L.Ed. 1186 (1918); *McCann v. New York Stock Exchange*, 80 F.2d 211, 213 (2<sup>nd</sup> Cir.  
14 1935). The fact that the offending conduct occurred in another courtroom means only that there are two  
15 courts with the power to set things right rather than just one.

16 It is the impact of counsel’s statements on the administration of justice which causes the court to  
17 treat this matter so seriously. Bankruptcy courts and state courts interact with each other on a frequent  
18 basis. It is imperative that each have faith in the judgments and orders of the other in order to avoid  
19 situations where litigants can routinely collaterally attack the rulings of one court in the other. This court  
20 considers it of the highest importance that all of the state courts within its territory know that all rules  
21 regarding notice, and due process rights generally, are scrupulously enforced. Proper notice is the *sine*  
22 *qua non* of any order this court has ever made. The court itself checks the sufficiency of every service.  
23 Lanahan & Reilley had no business falsely representing otherwise to another court.

24 The court does not believe that the conduct of Lanahan & Reilley rises to the level of criminal  
25 contempt. It seems that the basic cause of the misrepresentations made to the state court were Torbohn’s  
26 lack of understanding of bankruptcy procedure and her naive acceptance of her clients’ story.

1 Nonetheless, the bankruptcy docket clearly reflects due notice to her clients. It was her responsibility to  
2 ascertain that fact and disclose it to the state court when making her argument to it that her clients never  
3 got notice. Due to her failure to act properly, the estate incurred expense in having to pay for an  
4 appearance in state court and confidence in this court's orders was diminished. The court determines it  
5 to be a proper exercise of its inherent civil contempt powers to set things right.

6 For the foregoing reasons, the court will order as follows:

7 1. The bankruptcy estate incurred \$2,600.00 in legal fees when the Trustee's attorney was forced  
8 to appear in state court and set the record straight regarding the bankruptcy notice. This would not have  
9 been necessary if Lanahan & Reilley had made a proper review of the bankruptcy file and made the  
10 proper disclosures to the state court. The court finds it necessary to compensate the estate for this  
11 expense, plus \$325.00 for making the motion. Lanahan & Reilley shall therefore be ordered pay the  
12 Trustee the sum of \$2,925.00, and shall be barred from appearance in this court until this sum has been  
13 paid.

14 2. The court will assess a fine against Jennifer E. Torbohn in the amount of \$5,000.00, to be paid  
15 to the Clerk of the Court within 30 days of the entry of an appropriate order. Provided, however, that the  
16 court will remit and forgive all but \$500.00 of this fine if within that 30-day period she writes a letter to  
17 the Honorable Michael B. Dufficy, Judge of the Marin County Superior Court, with a copy to the  
18 undersigned, admitting to him that the bankruptcy court docket reflected proper service of the notice of  
19 compromise on her clients, that she had a duty to ascertain that fact and disclose it when making her  
20 argument that her clients had not received notice, and that she breached her duty to that court by failing to  
21 so ascertain and disclose.

22 Counsel for the Trustee shall submit an appropriate form of order.

23 Dated: November 22, 2004

24   
25 Alan Jaroslovsky  
26 U.S. Bankruptcy Judge